

Estonia

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1 Setting the Scene - Sources and Overview

1.1 What are the main corporate entities to be discussed?

The single type of corporate entity in Estonia, the shares of which are publicly tradable, is a public limited liability company ("PLC" or "company"). The minimal size of the share capital of a PLC is EEK 400,000 (approx. EUR 25,600). Of the total number of approx. 114,000 corporate undertakings registered in Estonia (as at 1 January 2008), PLCs account for approx. 5%, whereas private limited liability companies account for approx. 75%.

1.2 What are the main legislative, regulatory and other corporate governance sources?

The legal environment of the corporate governance is set by the Commercial Code, which includes most of the regulation related to day-to-day management of companies.

Other main sources of corporate governance regulation include the Law of Obligations Act; the General Principles of the Civil Code Act; the Estonian Central Register of Securities Act; the Competition Act; the Securities Market Act; and the Credit Institutions Act.

In addition to the abovementioned legal acts, other main sources of corporate governance rules include the Tallinn Stock Exchange Rules, issued by the Tallinn Stock Exchange, and the Corporate Governance Recommendations (hereinafter the "CGR"), issued by the Financial Supervisory Authority in co-operation with the Tallinn Stock Exchange. The former is mandatory for listed companies whereas the latter is mandatory on a comply-or-explain basis. The CGR are recommended but not mandatory for non-listed companies.

1.3 What are the current topical issues and trends in corporate governance?

The improvement of corporate governance is an on-going process in Estonia. The last time major changes were introduced in the regulations affecting corporate governance was in the beginning of 2007, when regulation on establishment of private limited liability companies online within one day was introduced; and the provisions concerning the registration of areas of activities of companies were changed and simplified - to name a few. In addition, as from 1 January 2006, all listed companies must follow the CGR on a comply-or-explain basis. The introduction of the CGR is a vehicle for implementing the good corporate governance

principles in Estonia to the extent not governed by the law. Other recent changes from the corporate governance side have mainly been part of the constant progress.

2 Shareholders

2.1 What rights and powers do shareholders have in the operation and management of the corporate entity/entities?

The shareholders have all basic shareholder rights, including the right to obtain information on the company on a timely and regular basis; the right to participate and vote in the shareholder meetings; the right to elect supervisory board members; and the right for a share in the profits of the company.

The shareholders' rights in a company are exercised through the general meeting. A general meeting is exclusively competent to amend the articles of association, increase and reduce share capital, issue convertible bonds, elect and remove members of the supervisory board, elect an auditor, designate a special audit, approve the annual accounts and distribute profit, decide on dissolution, merger, division or transformation of the company, decide on conclusion and terms and conditions of transactions with the members of the supervisory board, decide on the conduct of legal disputes with the members of the management board or supervisory board, and appointment of the representative of the company in such transactions and disputes; and decide on other matters placed in the competence of the general meeting by law.

The general meeting's competence cannot be amended by the articles of association. However, a general meeting may still adopt resolutions on other matters related to the activities of the company at the demand of the management board or supervisory board. It should be noted though that in such case the shareholders shall be jointly and severally liable in the same manner as members of the management board or supervisory board for damage caused by resolutions adopted under such conditions.

2.2 Do indirect shareholders (e.g. beneficial shareholders who hold through nominees), have direct rights in relation to the corporate entity/entities?

Under Estonian law, only direct shareholders have rights in relation to corporate entities. The control of the beneficial shareholders over the corporate entities can be exercised through the direct shareholders.

2.3 Are there any limitations on, and disclosures required, in relation to interests in securities by shareholders?

As to the speed of acquiring securities or the maximum amount of shares held by a shareholder, no regulatory limitations exist which would fit in the scope of the present questionnaire. However, the provisions of mandatory takeover need to be taken into account in case of a listed company. One should also consider the restrictions imposed by the insider trading related provisions.

As to disclosure, together with the annual accounts the company must present the list of shareholders who own more than 10% of the votes represented by the shares whereas such level for listed companies is 5% of the votes represented by the shares.

If all the shares in a company belong to one single shareholder or if, in addition to the single shareholder, the shares of the company are owned only by the company itself, the management board shall immediately submit a corresponding written notice to the Commercial Register.

Further, a person acquiring, directly or indirectly, the number of votes in a listed company up to or more than 5, 10, 15, 20, 25 or 50% or up to or more than 1/3 or 2/3 of all the votes represented by such issuer's shares shall notify the issuer of such acquisition within four trading days. The issuer will disclose respective information according to applicable rules. The same obligation of disclosure applies in case the number of votes of a shareholder in an issuer falls below the said thresholds.

Certain disclosure obligations are also imposed on a listed company acquiring or transferring its own shares.

2.4 What shareholder meetings are commonly held?

In PLCs, it is compulsory to hold ordinary annual general meetings of shareholders, which meeting is called by the management board no later than after six months from the end of the previous financial year (nevertheless, allowing the term to expire does not affect the validity of the resolutions passed at the meeting). While at the ordinary general meeting, the shareholders usually decide on the approval of the annual report and the distribution of dividends, the passing of other resolutions at the ordinary general meeting is not uncommon.

The management of a PLC will call an extraordinary general meeting of shareholders in case:

- i) the company's net assets have fallen below half the amount of the share capital or less than the minimum share capital required by the law;
 - ii) it is required by the shareholders whose shares represent at least one-tenth of the share capital;
 - iii) it is required by the supervisory board or the auditor; or
 - iv) it is evidently necessary for the interests of the company.
- (See question 2.5 below for voting and passing resolutions.)

2.5 Can shareholders call shareholder meetings or put resolutions?

The management board must call extraordinary shareholder meetings upon the request of shareholders holding at least one-tenth of the share capital. In case the management board does not call a meeting upon such shareholders' request, the shareholders can call the meeting themselves.

Shareholders whose shares represent at least one-tenth of the share capital may demand the inclusion of a certain issue on the agenda of the meeting (in case some issue has not been included in the

agenda, it may be inserted to the agenda at the meeting only if nine-tenths of the shareholders present at the meeting give their consent thereto and if the aforementioned nine-tenths of the shareholders hold at least two-thirds of the share capital).

A resolution of the general meeting shall be adopted if over one-half of the votes represented at the meeting are in favour, unless a greater majority requirement is prescribed by law or the articles of association. Resolutions on certain material issues, e.g. amending the articles of association, changing the amount of the share capital, merger, division and reorganisation of a company shall only be adopted if at least two-thirds of the votes represented in the meeting are in favour unless a greater majority requirement is stipulated by the articles of association.

2.6 Is electronic communication to or by shareholders possible?

The shareholders may choose to perform the resolution-taking process electronically provided that all shareholders are in favour of the resolutions being adopted and such resolutions are signed with digital signatures (holding an Estonian identity card is required). In all other cases a meeting has to be called.

The management may call a general meeting of shareholders by an electronic notice of the meeting provided that the notice concerning the obligation to immediately send acknowledgement of receipt of the document is appended to the notice.

Certain basic corporate actions which require registration with the Commercial Register, and which could formerly only be carried out by making notarised applications (such as founding of private companies, submission of annual reports, changing corporate data, etc.) can be carried out by means of using the electronic portal for undertakings (in Estonian: "Ettevõtjaportaal"), provided that the persons using the portal hold Estonian identity cards. Although a rather novel (and constantly evolving) solution not wholly without setbacks, it has already won numerous supporters, especially for making life easier for the management side. Nevertheless, from the shareholder's point of view, one can hope for further improvements.

2.7 Can shareholders be liable for acts or omissions of the corporate entity/entities?

As a general rule, only the company itself can be held liable for any shortcomings in its organisation or otherwise. The shareholders' liability for the company's acts or omissions is limited to their shareholding size in the company.

Nevertheless, a shareholder is liable for the damage that he has wrongfully caused to the company, another shareholder or a third person as a shareholder. A shareholder shall be released from liability if he has not participated in adopting the resolution of the general meeting by which the damage was caused or in case he voted against such resolution.

2.8 Can shareholders be disenfranchised?

While a shareholder can be excluded from a private limited liability company upon the request of other shareholders (and upon the occurrence of other conditions), it cannot be done in public companies except in case of exercising the general takeover of shares for monetary compensation by a shareholder holding the shares representing at least nine-tenths of the share capital.

2.9 Can shareholders seek enforcement action against members of the management body?

The shareholders and the company have the right to seek enforcement action against members of the management board and/or the supervisory board in the event of a breach of board member's obligations.

(See also question 3.7 below.)

3 Management Body and Management

3.1 Who manages the corporate entity/entities and how?

The day-to-day management is carried out by the management board (sometimes also referred to as the "board of directors"). In the PLCs, a two-tier system of management is used: it is compulsory to have in addition to the management board a supervisory board that plans the activities of the company, organises the management and supervises the activities of the management board.

The supervisory board gives instructions to the management board for organisation of the management of a company. The consent of the supervisory board is required for conclusion of transactions which are beyond the scope of everyday economic activities and, above all, for conclusion of transactions which bring about the acquisition or termination of holdings in other companies, the foundation or dissolution of subsidiaries, the transfer or encumbrance of immovables or registered movables, the making of investments or the assumption of loans exceeding a prescribed sum of expenditure for the current financial year, etc. A member of the supervisory board need not be a shareholder.

A member of the management board must be a natural person with active legal capacity. At least one half of the members of the management board must have their residence in Estonia, in another Member State of the European Economic Area or in Switzerland.

Every member of the management board may represent the company in all legal acts unless the articles of association prescribe that some or all of the members of the management board shall represent the company jointly. Joint representation shall apply with regard to third persons only if it is entered in the Commercial Register.

From the perspective of a third person, the division of duties and areas of responsibility of managers do not affect the managers' rights of representation, with the exception of joint representation described in the above passage.

3.2 How are members of the management body appointed and removed?

Members of the supervisory board are elected and removed by the shareholders' general meeting. It may be stipulated by the articles of association that not more than half of the members of the supervisory board are elected or appointed and removed in a different way (e.g. appointed by a certain shareholder, etc.). The respective resolution is submitted to the Commercial Register by the management board, along with the list of supervisory board members and the written consent of the prospective supervisory board member. From among its members, the supervisory board elects a chairman who takes care of the administrative issues in the workings of the supervisory board.

Supervisory board members are elected for five years unless the articles of association stipulate a shorter term of office.

The election and removal of management board members is carried out by the supervisory board. The resolution of the supervisory board on election or removal of management board members is submitted to the Commercial Register, along with a notarised application signed by the elected board member and the chairman of the supervisory board.

The members of the management board are elected for three years unless the articles of association stipulate another term of office (which cannot, however, be longer than five years).

3.3 What are the main legislative, regulatory and other sources impacting on directors' contracts and remuneration?

According to the Commercial Code, the amount of remuneration payable to a member of the management board and the conclusion of a contract with a member of the management board shall be determined by the supervisory board. Upon determining the procedure for remuneration of the members of the management board and the amount of fees and other benefits, and upon concluding contracts with the members of the management board, the supervisory board shall ensure that the total amount of the payments made by the company to the members of the management board are in reasonable proportion to the duties of the members of the management board and the economic situation of the company.

If the economic situation of a company significantly deteriorates and further payment to a member of the management board of the fees established for or agreed upon with the member, or further allowing of other benefits to the member would be extremely unfair to the company, the company may require the decrease of the fees or benefits. If decrease of fees or other benefits is demanded, the member of the management board may exercise the right to extraordinary cancellation of a contract concluded with him or her upon one month's advance notice of cancellation.

3.4 What are the limitations on, and what disclosure is required in relation to, interests in securities held by members of the management body?

The Tallinn Stock Exchange Rules stipulate rather strict rules for the purposes of avoiding inside trading including a prohibition on the members of the management bodies and persons related to them to trade in the issuer's securities with the purposes of gaining profit on short-term fluctuation of share prices and during the prohibited periods set forth by the Rules. The management bodies' members as insider shall adhere to all other rules relating to restrictions on transactions by insiders and disclosure relating thereto.

The members of the management bodies are obliged to disclose to the company information on their interests and transactions in securities of the company.

3.5 What is the process for meetings of members of the management body?

On the management board level, the method of taking resolutions is to be determined internally in the company. Such method may be required (and regulated) by the supervisory board, or it may be set up internally by the management board. Special internal regulations for the workings of the management board usually exist in larger corporations with many board members, especially in case duties are divided within the management board.

Supervisory board meetings are held when necessary, but not less frequently than once every three months. A meeting shall be called

by the chairman of the supervisory board or by a member of the supervisory board substituting for the chairman. Advance notice of at least one day shall be given of the holding of a meeting and of its agenda unless the articles of association prescribe a longer term.

A meeting of the supervisory board has a quorum if more than one-half of the members of the supervisory board participate (here again, the articles of association may prescribe a greater representation requirement).

A meeting of the supervisory board shall be called if this is demanded by a member of the supervisory board, the management board, an auditor or shareholders whose shares represent at least one-tenth of the share capital. If the meeting is not called within two weeks after the date of receipt of the relevant request, a member of the supervisory board, the management board, auditors or shareholders have the right to call the meeting themselves. An issue which is not included on the agenda in the notice may be added to the agenda by the supervisory board only if all members of the supervisory board participate in the meeting and at least three-quarters of the members of the supervisory support including the issue on the agenda.

Minutes shall be taken of a meeting of the supervisory board. The minutes are signed by all members of the supervisory board who participate in the meeting and by the recording secretary of the meeting. The dissenting opinion of a member of the supervisory board shall be entered in the minutes, which shall be confirmed by his or her signature.

If the requirements of law or of the articles of association are violated in the calling of a meeting of the supervisory board, the supervisory board shall not be authorised to adopt resolutions unless all the members of the supervisory board participate in the meeting. Decisions made at such meeting of the supervisory board are void unless the members of the supervisory board with respect to whom the procedure for calling the meeting was violated approve of the decisions.

3.6 What are the principal general legal duties and liabilities of members of the management body?

The principal obligations of management and supervisory board members include the performance of his or her duties with due diligence, being loyal to the company, the preservation of the business secrets of the company and the adherence to the prohibition of competition. Members of the management and supervisory board who cause damage to the company by violation of their obligations shall be jointly and severally liable for compensation for the damage caused. A board member is released from liability in case he or she proves that he/she acted with due diligence.

The limitation period for assertion of a claim against a member of the management board and the supervisory board is five years unless the articles of association or an agreement with the member of the board prescribes another limitation period.

A claim for payment of compensation to a company for damage caused due to a breach of a board member's obligations may also be submitted by a third person if the assets of the company are not sufficient to satisfy the claims of such third person.

3.7 What are the main specific corporate governance responsibilities/functions of members of the management body?

The management board is responsible for everyday management of the company i.e. for organising the accounting, preparing the general meetings of shareholders, concluding agreements with

clients, employees and other third persons, preparing annual accounts, etc.

The management board also guarantees the application of necessary measures and above all, the performance of internal audit in order to detect, as early as possible, any circumstances which likely to pose a danger to the operation of the public limited company.

The supervisory board supervises the activities of the management board, grants approvals for concluding transactions beyond everyday business activities, presents to the general meeting a written opinion on the annual report prepared by the management board, etc.

3.8 What public disclosures concerning management body practices are required?

According to the CGR, the division of tasks regarding the management of the company must be disclosed in respect of the management and supervisory boards to the extent not already provided in the articles of association. Upon changing the division of tasks the company shall publish the content of the change, the effect to the company and the period of implementation of the change.

The CGR set forth that the notice on calling of a general meeting has to be published on the company's website simultaneously with sending the notices out to the shareholders as well as relevant information pertaining to the agenda of the general meeting. In addition, the supervisory board shall disclose its opinion on the item on the agenda of the general meeting.

3.9 Are indemnities, or insurance, permitted in relation to members of the management body and others?

Whilst insurance of management body or other corporate structures is permitted, so far it has not become a common practice in Estonian companies, except for in certain larger corporations.

4 Corporate Social Responsibility

4.1 What, if any, is the law, regulation and practice concerning corporate social responsibility?

With no laws concerning corporate social responsibility, corporate social responsibility has thus far not become a serious factor in the Estonian corporate sphere on a regulated level. Nevertheless, quite a few companies have started organising public sporting events, now and then some companies (especially in the finance sector) can be seen supporting hospitals, museums, etc. The tendency seems to be in the direction that companies earning bigger-than-average profits are contributing to the social sphere via direct funding or via participation in charity events and the like.

4.2 What, if any, is the role of employees in corporate governance?

The employees do not have a specific role in corporate governance.

5 Transparency

5.1 Who is responsible for disclosure and transparency?

By and large, the spheres of disclosure and transparency are the responsibility of management board.

5.2 What corporate governance related disclosures are required?

For all companies, it is compulsory to prepare and disclose annual reports, the key purpose of which is to give a true and fair view of the financial position, economic performance and cash flows thereof.

The CGR require that in the CRG report (which forms a separate chapter in the annual report), inter alia, the following data about the company be disclosed: management and supervisory board remuneration conditions; the transactions made between the company and a management board member, if approved by the supervisory board; and the attendance frequency of supervisory board meetings by a member of the supervisory board.

5.3 What is the role of audit and auditors in such disclosures?

The main role of auditors is to evaluate whether the disclosures reflect the actual standing of the company and whether required accounting practices have been followed.

An auditor's opinion is required for annual accounts of a PLC. The auditor is elected by the general meeting for a specified term or a single audit. The general meeting also determines the terms of the auditor's remuneration. There is no general requirement for rotation of the auditors in place; however, an individual executive/responsible auditor of a company subject to financial

supervision must not audit the same company for more than five years in a row. The CGR set forth certain requirements to the auditor's independence; the law however does not contain any special provisions in that respect.

5.4 What corporate governance information should be published on websites?

According to the CGR, the website of a company must be clear in structure and published information should be easy to find. Published information must also be available in English. A company must publish the disclosure dates of information subject to disclosure throughout a year (including the annual report, interim reports and notice calling a general meeting) at the beginning of the fiscal year in a separate notice, which is referred to as the "financial calendar".

CGR also stipulates that the following be accessible to the shareholders on the company's website: CGR report on Corporate Governance Recommendations; information on the following general meeting; articles of association; general strategy directions of the company as approved by supervisory board; membership of the management board and supervisory board; information regarding the auditor; annual report; interim reports; agreements between shareholders concerning concerted exercise of shareholders rights (if those are concluded and known to the company); and other information, published on the basis of CGR.



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